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C O P Y

OFFICE CORRESPONDENCE

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To Governor Szymczak

Subject: The Treasury's plan for a world Stabilization Fund

From Walter R. Gardner

This is the story of the Treasury's plan for a world Stabilization Fund. A similar plan prepared by Lord Keynes was the subject of a more detailed analytic memorandum last December, but revisions of the Keynes plan have necessitated revisions of the memorandum which have not yet been completed. The Treasury plan itself has undergone a series of changes and more are in prospect. Meanwhile the present memorandum will give the essential facts of the case.

Formation of committees under Treasury leadership

On May 15, 1942 the Secretary of the Treasury sent a communication to the President enclosing a long memorandum by Harry White. The memorandum proposed establishment of a world Stabilization Fund and a world Bank. The Secretary requested the President to authorize the Treasury to continue its work on this proposal with the aid of the Department of State, the Federal Reserve Board, and the Board of Economic Warfare with a view to calling a conference in Washington of the Finance Ministers of the United and Associated Nations. The President approved continuance of the study; but in directing the Treasury to cooperate with other agencies in the Government he named specifically the State Department, the Board of Economic Warfare and the Export-Import Bank, and failed for some reason to mention the Federal Reserve Board. Nevertheless Secretary Morgenthau wrote Chairman Eccles on May 20 requesting his cooperation in working out the proposal. A meeting was called for May 25 at which Secretary Morgenthau presided. The Chairman and Mr. Goldenweiser attended for the Board, and the other agencies already mentioned were represented by high officials. It was agreed that the project was of major importance and that members of the technical staffs of the agencies represented should continue the study under the chairmanship of Harry White.

Question of an international conference

In the meetings of the technical group which ensued the Federal Reserve Board was represented by Messrs. Goldenweiser, Hansen, and Gardner. Harry White was chiefly interested in getting the group to agree that an international conference should be called on his proposal for a world Fund and Bank. Mr. Goldenweiser, with the approval of the Board, took the position that the basic post-war objective was physical reconstruction to which financial arrangements must be adapted, and that it was necessary to make the best forecasts we could of the economic needs of the world before we could determine what new types of financial machinery would be required to service those needs. He felt that we were not yet in position to conclude that a Stabilization Fund and a Bank were called for nor could we intelligently discuss the organization of such institutions without having taken the measure of the job to be done.

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The Treasury people were somewhat impatient with this line of argument, since they regarded it as certain that currencies would have to be stabilized in some measure by action of the monetary authorities, that international action to this end would be more promising than unconcerted national policies, that a world Stabilization Fund would therefore prove to be one of the necessary institutions, and that it was desirable to attack post-war financial problems wherever a beginning could most easily be made in hopes that other necessary steps would follow. The Treasury people felt that establishment of a world Fund would help to clear the way for these other more difficult steps if only because it would establish an organized working relationship in the field of finance among the participating Governments. It was apparent that the Treasury was really using the group to smoke out the State Department on the question of an international conference.

On this question of an immediate international conference Mr. Berle of the State Department finally put a quietus in the meeting of July 10. In view of the heavy defeats that were then occurring in Africa and Russia, and the appearance of submarines practically in our harbors, he felt that a conference of the United Nations to discuss details of what they were going to do with the victory would appear to the public a little bit like "building castles in Spain". He recalled the difficulty that proposals for sweeping international collaboration had always encountered in this country. The specious objection would be raised in many quarters that we were not only fighting the war for other countries but planning to give the United States to the world afterwards, and he suggested that the most carefully considered strategy would have to be employed to get the proposal adopted by the American people. The fixing of a date for the conference now might, he felt, find us way out on a limb when the time for the meeting arrived.

He then turned to the Treasury proposal that thirty-six countries should participate in the discussions. A number of the countries that were expected to play a significant role were frankly hollow shells. The exiled governments of occupied countries were useful symbols but what would come out of the ferment which their peoples were experiencing was quite unpredictable. It was highly unlikely that most of these exiled governments would ever be reinstated. Certainly they could not now give any effective commitment as to the post-war policies their peoples would follow. Many other countries in the long list proposed by the Treasury, including most of the Latin American countries, were hardly in position to contribute much to the discussion.

Mr. Berle agreed that for the discussion to be effective specific proposals must be put up for consideration. His suggestion, however, was that no formal conference be contemplated at that time. Instead, discussions should proceed with competent technicians already in Washington of countries that might be expected to play a significant role. Memoranda could be exchanged with these men; and although the discussions might be bilateral, the fact could be made clear that a group and not just a single country was being consulted. As the discussions proceeded, the stage might be reached at which the measure of agreement within the group and the general war situation would make it apparent that the time had come for calling a more formal conference of those who were in position to commit their countries. While an effort should be made to keep the preliminary informal

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discussions as quiet as possible, it was probable that some suggestions of what was going on would sooner or later get out to the newspapers, and the reaction to these partial leaks might prove helpful in determining when the time was ripe for more formal negotiations. For the time being it was important that we should not tie our hands. At several points in his remarks Mr. Berle stated emphatically that he was personally eager to get ahead with specific action in this field, as those present undoubtedly knew.

Mr. White was visibly impressed with the tone and substance of Mr. Berle's remarks and the meeting rapidly came to a head along the lines that Mr. Berle suggested. The question of fixing a date for a formal conference was dropped. A list of countries with which it would be useful to pursue informal discussions was made up, the countries selected being the United Kingdom, Russia, China, Canada, Australia, and Brazil. A broader list of countries would be kept informed of what was going on and might even be brought into the discussions in those cases where particular interest or competence was shown.

The Keynes Plan

Although the Berle proposal contemplated action, Harry White appeared to lose interest in the program during the summer months. No meetings were called. The whole project was brought to life again by the British. Phillips of the British Treasury sent Secretary Morgenthau on August 28 a proposal for an International Clearing Union. It had been prepared by Lord Keynes and had the approval of the British Government as a basis for discussion. The Keynes' plan, if put in operation, would be highly favorable to foreign countries like England which might wish to draw extensively upon the United States in the post-war period. It would add to the existing 10 billion dollars of foreign gold reserves perhaps as much as 25 billion dollars of new international reserves in the form of a new world currency convertible into national currencies. At the outset the new world currency reserves would be dealt out gratis to the participants in proportion to the total foreign trade of each. They could then be used as freely as gold in settling international transactions. It is contemplated that measures to correct the balance of international payments would be brought into play to render excessive use of the reserves unnecessary; but nevertheless foreign countries coming out of the war with severely curtailed standards of living would be under strong temptation to follow expansionist policies and to use their enlarged powers to purchase American goods, and it is conceivable that much of the possible 35 billion dollars of foreign gold and world currency reserves might flow to the United States as gold flowed in the 1930's. If it did, the effects upon the American banking system would be the same. Member bank reserves would be increased without the Federal Reserve System gaining any offsetting power. A considerable movement of this character might leave the System unable to meet its major responsibility of so handling the credit supply of the country as to contribute to the orderly development of the American economy.

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The Keynes plan was, therefore, of direct and major concern to the Federal Reserve Board. The Treasury sent copies to the Board on September 11 and a meeting of the White committee was called for September 18. There then ensued a series of meetings which resulted in a set of written questions being sent to the British on matters of interpretation while the broader implications of the Keynes plan were never comprehensively discussed.

Renewed consideration of the White plan

It was at this stage that the White plan began to come to life again in the form of a mimeographed summary. The first of these mimeographs was distributed at a meeting in November and a series of revised summaries appeared at later meetings. The latest of these bears the date of December 24, 1942. Attention was gradually diverted from the Keynes plan to these summaries; and under White's guidance they were given a swift going over section by section. The gatherings were often large, including individuals such as Ben Cohen and Lauchlin Currie in addition to staff members from the five agencies working on the project, and much of the discussion was either diffuse or hurried. After a few meetings of this sort what appeared to be only a preliminary sizing up of the plan was taken as group approval of it for purposes of discussion with other countries. A meeting of the main committee - the so-called "cabinet committee" on which Chairman Eccles is represented - was called to receive the recommendation of the technical committee to that effect.

Meeting in Secretary Morgenthau's office

Chairman Eccles did not attend this meeting, which occurred on December 15 and was presided over by Secretary Morgenthau. Instead, Governor Ransom went with Mr. Goldenweiser and Mr. Gardner. It developed at the meeting that the chief reason for hurrying forward the Treasury plan, which was still quite immature from a technical standpoint, was that the British were anxious to proceed with discussions of the Keynes plan abroad. They had already presented it to the Dominions at a meeting in London and were ready to start talks with the Russians and Chinese. Mr. Berle indicated that there might be danger of the center of discussion being transferred to London (instead of Washington) if the Americans appeared to leave the initiative to the British. The danger that Mr. Berle saw was, of course, exaggerated because all the plans for monetary stabilization that are being discussed depend for their success upon U. S. willingness to contribute the bulk of the funds, and therefore persuasion of the United States is the central strategy behind them all. The master discussions will certainly take place in Washington unless we choose to carry them on abroad. Nevertheless there may be some advantage in getting foreign thinking started as early as possible along lines that appear feasible to us instead of allowing it to crystallize around plans that we would have to veto because of the blank check they involve upon the resources of this country.

Mr. Gardner pointed out at the meeting that the Treasury plan itself would open the way to large drafts on the United States because it permitted foreigners to increase their subscriptions above the minimum required.

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Foreigners would be under strong inducement to do so because their gold reserves would command many times more foreign exchange if deposited with the Fund than they would if used directly for purposes of international settlement. As foreigners increased their subscriptions, their voting power under the plan would automatically be increased; and because of this the United States would be compelled to increase its own subscription in order to maintain control over more than 1/5 of the votes -- a control which under the plan would give it veto power over those major actions of the Fund that require a 4/5 vote. If foreigners went the limit in depositing their gold, foreign gold at the disposal of the Fund plus the U. S. contribution would amount to well over 20 billion dollars; and if this were used over a period of years to settle adverse balances with the United States -- a possibility which was not too remote in view of the fact that the world's needs would be backed with dollar purchasing power under the plan -- this country might find itself making a huge contribution to the rest of the world, the financial counterpart of which would be the addition of tens of billions of dollars to member bank reserves in this country without any corresponding increase in the offsetting power of the Federal Reserve Banks. This was the point of the question Mr. Gardner raised and of his subsequent remarks, though the story never got told to the end because Mr. White insisted that his plan contemplated an American contribution of only 2 to 2-1/2 billion dollars. His mind was evidently fixed on the original quota that the United States was required to subscribe. He took no account of foreign gold subscriptions, either required or voluntary, and no account of the subscriptions that the United States would have to make to retain its veto power; nor was it possible to clear the matter up in view of the general character of the meeting, which rendered prolonged technical discussion inappropriate.

Secretary Morgenthau stated that he had called the meeting in the belief that the technical committee was in agreement on the plan and wished his assistance in taking the next step, which was to ask Secretary Hull to approve talking it over at the technical level with the Russians, the Chinese, and officials of other countries. When he asked whether this was the sense of the meeting, Governor Ransom stated that, in the absence of Chairman Eccles, he would like to have an opportunity to consult him.

Understanding with the Federal Reserve Board

Upon their return from the meeting Messrs. Ransom, Goldenweiser, and Gardner went in to see the Chairman and it was agreed that there would be no objection to the discussions of the plan becoming international, provided Mr. Goldenweiser made it clear to Harry White that it was understood that a commitment of no more than 2-1/2 billion dollars was contemplated and that the text of the draft would be so modified as to leave no doubt on that score. Mr. Goldenweiser acted accordingly by telephone on December 15 and by confirmatory letter on December 16.

Harry White replied in a letter of his own on December 22, calling attention to the fact that foreigners might obtain more than the 2 or 2-1/2 billion dollars if they made requests that were approved by the American authorities, and Mr. Goldenweiser wrote back on December 23 that he believed himself and Harry to be in full agreement. In his letter of December 16 he had had reference only to the amount of dollars that this country could be compelled to supply.

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Even before this correspondence was completed a new draft of the Treasury plan was prepared on December 16 in which quotas were fixed -- i.e. they ceased to be merely a required minimum that could be increased at will to obtain additional voting power and rights to more assistance from the Fund. Any increase in quotas was made subject to a 4/5 vote of the Board of Directors, thus giving the United States a veto power. The point at issue was settled satisfactorily.

Extent to which gold flow and Fund operations might build up our member bank reserves

It is necessary, however, to guard against the impression that under the Treasury plan as now constituted international transactions could add only 2 to 2-1/2 billion dollars to member bank reserves. The Treasury plan commits this country to buying all gold offered to it at a price fixed by the Fund. While this is not stated in so many words in the language of the plan, Harry White agreed in the committee discussions that this was the effect of two of its provisions taken together. Under the plan the United States would be committed to maintain by appropriate action the exchange rates established by the Fund on the currencies of other countries. The Fund would also fix the rates of local currencies in gold. Hence a country that refused gold offered at the fixed price would be defaulting on its obligation to maintain exchange rates unaltered.

Foreign gold reserves are much greater today than they were at the peak in the 1920's. In dollar value they are more than 10 billion dollars as against 5 billion in 1929. And world gold production is running at 1,300 million dollars a year as against 400 million in the 1920's. All of this more than 10 billion dollars of foreign gold reserves plus perhaps 5 billion dollars of new gold production could conceivably be added to United States gold stocks during a period of four years. Such a possibility is remote, of course, because foreign countries would not allow themselves to be stripped of gold; but if they allowed their gold reserves to be cut back only to the peak figure of the 1920's the U. S. gold stock could still increase by more than 10 billion dollars. The 2 billion dollar U. S. contribution to the world Fund plan would come on top of that, probably taking the form of rendering active the inactive gold in the U. S. Stabilization Fund. All these newly created dollars would add to member bank reserves without adding to the offsetting power of the Federal Reserve System.

It is perhaps the chief virtue of the Treasury plan that it sets up an international body with the right to inquire into the causes of exchange disequilibrium and to make recommendations that will carry weight because they carry dollars with them. Our contribution of 2 billion dollars might be regarded as payment for the power to influence the balance of international payments. True, such influence might well be obtained without any payment at all. The world is anxious to have the right to convert its gold into dollars and to get the fruits of American productivity which that makes possible. If we intimated that we might have to reconsider our gold buying policy unless an international agency were created to keep exchange rates in proper balance and to recommend measures designed to minimize the gold flow, the international agency would probably come into existence. Reconsideration of our gold buying policy would not mean a threat of complete

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stoppage -- merely something on the model of the British Fund with discretionary, rather than automatic, buying of gold and an exchange policy that permitted an orderly decline of foreign currencies relative to the dollar. The Treasury plan which commits us to buying all of the more than 10 billion dollars of foreign gold reserves that is offered and then throws in another 2 billion in purchasing the influence to check the movement will probably not be so quick-acting and will create greater problems for the Federal Reserve System; but it may be more agreeable to foreign countries and therefore easier to set up.

<u>The quota: basis of a country's contribution, its vote, and its right to assistance from the Fund</u>

Contributions to the Fund will be made by Governments. It is suggested that the aggregate subscription should be at least 5 billion dollars. Each country's subscription will be determined by its quota. The quota will be based on a long list of factors such as the country's gold and foreign exchange holdings, the magnitude of the fluctuations in its balance of international payments, its national income, foreign trade, population, etc. Just how these different elements will be combined to reach some common figure for the quota is left uncertain. Yet the quota is basic to the whole plan, for it not only determines what a country shall subscribe, but also the amount of assistance which the country can freely obtain from the Fund. The initial subscription of 50 per cent of the quota will be made to the extent of 12-1/2 per cent of the quota in gold, 12-1/2 per cent in national currency, and 25 per cent in interest-bearing bonds of the national government. Countries with less than 300 million dollars of gold need pay in only 7-1/2 per cent of their quota in gold; and countries with less than 100 million dollars, only 5 per cent -- the difference being made up by a larger contribution in national currency. The burden on a country's gold reserves of subscription to the Fund is, therefore, light. Since the Fund must assist the country with foreign exchange up to the full amount of its quota, the larger a country's quota, the more it gains in power to settle an adverse balance of international payments. That is why the formula adopted for determining quotas is of critical importance. But the only certainty about it at the moment is that the United States must insist that ingredients in the formula shall be so concocted as to give this country a quota of about 2 billion dollars out of a total of 5 billion. A subscription of this size is needed to insure the United States enough of a vote to veto decisions requiring a 4/5 majority.

<u>Voting power, with particular reference to the veto</u>

The voting system may be briefly explained. The Government of each country appoints one member of the Board of Directors which manages the Fund. Each director has 100 votes plus 1 vote for every 1 million dollars of his country's quota (i.e. its full quota even though only half may have been paid in). No director, however, may cast more than one-fourth of the aggregate votes. The United States would, therefore, have no interest in acquiring more than one-fourth of the voting power. On the other hand it is essential that it acquire something over one-fifth of the voting power because this will give it a valuable veto over those major actions of the Board that require a four-fifths vote. A four-fifths vote is required:

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a. To call up the second half of the subscription -- i.e. the United States could prevent the second half being called up and thereby limit its contribution to the amount of the first half, if such action did not look like bad faith;

b. To change quotas of member countries -- i.e. the United States could prevent an enlargement of foreign quotas that would increase the foreign vote and the right to demand dollars;

c. To alter exchange rates and the price of gold -- i.e. the United States could prevent the Fund altering dollar exchange rates or the gold value of the dollar, and it could determine whether or not foreign countries would be allowed to alter their rates;

d. To borrow national currencies -- i.e. the United States could prevent the Fund borrowing in our market if it runs out of dollars;

e. To put currency held by the Fund into one-year loans to member Governments or into short-term commercial and Government securities -- i.e. by exercising its veto power from the outset the United States could prevent the Fund engaging in credit and open-market operations other than the sale of a country's bonds originally subscribed;

f. To establish the rules and regulations of the Board or to delegate Board powers to officers or committees during the intervals between meetings -- i.e. the United States could prevent any monkey tricks in the Board's operational procedure.

All these and one or two other powers of lesser significance may be wielded by the United States if it acquires more than one-fifth of the total vote. If there are 50 member countries with 100 votes each by reason of their membership, and aggregate quotas amount to 5 billion dollars with one vote for each 1 million dollars, the total number of votes will be 10,000. To give the United States a veto power its quota would have to be at least 2 billion dollars. The quota would then entitle the United States to 2,000 votes which, together with the 100 votes it receives as an attribute of membership, would be slightly more than one-fifth of the total vote.

While the veto power is of major importance, it is, of course, negative only. Positive action by the Fund could not be dictated by the United States because the maximum voting power that any country is permitted to acquire is one-quarter of the whole. By acquiring such power, however, the United States would be half-way toward the control of a majority vote and if most of the Latin American countries followed its lead this country might find itself with a working majority quite apart from the attitude of the rest of the world. Needless to say the Keynes plan is wholly different on this point. Keynes would distribute voting power as he

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does the right to draw upon the Clearing Union -- namely, on the basis of a country's foreign trade. The great trading countries -- notably the British Commonwealth itself -- would be the major powers in his arrangement.

Right to assistance from the Fund

Under the Treasury plan the Fund may, by majority vote, fix the initial gold value of currencies and their exchange rates with one another. Subsequent changes require a four-fifths vote. At the rates fixed a member country has the right to purchase foreign currencies from the Fund with its local currency up to the full amount of its quota for the purpose of meeting an adverse balance of international payments on current account. The limitation to "current account" means that the country could not obtain foreign exchange from the Fund to protect its currency from depreciation caused by an outward capital movement. Even amortization payments would have to be carefully separated out. With balance of payments data in the state they are in (witness the huge unexplained residual even in the United States accounts) it is not at all clear how the Fund could determine promptly and accurately what aid is lawful. Nor is it apparent why constructive capital movements should not be permitted to be handled smoothly in the exchange market without disturbing the values of the currencies involved. Such control of capital movements as is desirable should certainly be handled by other measures than one which hits out indiscriminately, which is hardly feasible administratively, and which may destroy the very exchange stability that the Fund is set up to achieve.

Power of the Fund to give assistance

While a country has the right to demand foreign currencies from the Fund up to the full amount of its quota to meet an adverse balance on current account, the Fund is not under obligation to sell a foreign currency if it does not have it and cannot obtain it. When demand for a currency threatens to exhaust the Fund's supply, the Fund may ration it according to its judgment of the needs of the would-be buyers; but it must make every effort to meet the demand.

Suppose, for instance, that the demand is converging on dollars. The Fund might first use up the original U. S. contribution of dollar currency; next it might convert into dollars its gold holdings from whatever source they have been received; then it would cash its dollar bonds although the plan is not clear as to the method. Beyond this the Fund might take advantage of the fact that every country must agree under the plan to offer for sale to the Fund all gold and foreign exchange in excess of the amount it possessed at the time it became a member. The Fund could force countries to sell it their "excess" dollars or gold convertible into dollars. If dollars still remained in short supply, the Fund could borrow dollars in the United States provided the United States was willing and some Government agency or the general market was prepared to lend. In addition the Fund would be under obligation to recommend measures to the United States designed to correct the shortage of dollars and the United States in turn would be under obligation to give immediate and careful consideration to those recommendations. All these methods would have to be employed by the Fund in order to reduce to a minimum the need for rationing United States currency.

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If, however, the Fund is adequately supplied with resources, it can not only satisfy the demands of countries exercising their rights to buy up to 100 per cent of their quotas; it can at its discretion go farther and supply additional amounts of foreign currency. It has the power under the Treasury plan to sell foreign for local currency until its net acquisitions of the latter reach 200 per cent of the quota of the nation whose local currency is being acquired -- or, more precisely, the limit is 100 per cent of the quota in the first year of operation; 150 per cent in the second year; and 200 per cent thereafter. The Fund can, for example, sell foreign currencies for sterling until its net acquisitions of sterling reach 200 per cent of the British quota.

Even this 200 per cent may be exceeded temporarily. If the country which is experiencing the adverse balance of payments is prepared to carry out the measures recommended by the Fund to correct its position, and if the Fund is convinced that the adverse balance will prove to be of short duration, there is no limit to the assistance that the Fund can give on current account. When the Fund gives assistance to a country, however, that country must deposit a special reserve and pay a charge of 1 per cent per annum on all of its currency acquired by the Fund in excess of the country's quota.

Release of blocked balances

Quite apart from any of these limitations the Fund can employ its resources to release blocked balances. There may be comparatively little for the Fund to do in this field. The United States will have no difficulty in releasing the 2-1/4 billion dollars of blocked balances here whenever it considers it advisable so to do. Its gold holdings are ample to meet any withdrawals. England and some other countries, however, may find it more of a problem. Blocked balances in England now amount to about 3 billion dollars; and, although under war-time Lend-Lease we are permitting England to build up its gold reserves to perhaps 1 billion dollars, that sum might not prove sufficient to permit the freeing of blocked balances unless amounts due to the Dominions and other Empire countries are cancelled or funded by agreement. But it seems probable that Empire balances will be handled in some such way, and if they are, the bulk of the 3 billion dollars will disappear. The problem of blocked balances should not, therefore, be exaggerated. The machinery set up for dealing with it in the Treasury plan is needlessly cumbersome and no purpose would be served by describing it in detail. The Federal Reserve is prepared to suggest a much more simple procedure. Suffice it to say that the essence of the arrangement is that the Fund will stand ready to take over the blocked balances, giving free currency in exchange, and that the blocked balances in the hands of the Fund will then be set free gradually over a period of not more than 20 years. Thus Argentina's blocked sterling could be made immediately available to her without putting any sudden strain on England. The immediate strain would all come on the Fund's resources, but would be gradually passed over to England as the blocked sterling is freed.

As the plan is now drafted England would not be obliged to free blocked sterling by this method. That would be a matter for negotiation between England, Argentina, and the Fund. All countries are committed under the plan, however, to abandon all restrictions and controls over

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foreign exchange transactions (other than those involving capital transfers) as soon as they decide that conditions permit. If they are laggard in this respect the Fund is authorized to make representations to them. No new restrictions can be imposed, nor can any bilateral clearing arrangements be adopted, without the approval of the Fund.

Commitment to cooperate in the control of capital movements

The exception of capital transfers from this free exchange commitment is significant. The Treasury plan contemplates control of capital movements. Each member country agrees to discourage the unnecessary accumulation of foreign balances by its nationals. Further, all countries will be committed under the plan to cooperate with other member countries which are attempting, with the approval of the Fund, to control capital movements more broadly. Among the measures that these cooperating countries must take upon recommendation by the Fund are:

a. Prohibit acquisition of deposits, securities, or investments in the cooperating country by nationals of the controlling country except with the permission of that country and the Fund;

b. Make available to the controlling country or the Fund full information on all property in the form of deposits, securities, or investments in the cooperating country held by nationals of the controlling country;

c. Adopt such other measures as the Fund may recommend.

As a major recipient of foreign capital, the United States would experience the full force of these commitments, and be under compulsion to devise and pass legislation adequate to meet its promises.

It may be noted that any really adequate control of capital transfers will involve general exchange control over goods and services as well as capital; for otherwise proceeds of merchandise exports or payments for services could readily be left abroad. While a general exchange control of this character could be administered (as in the present Canadian system) so as to leave trade transactions comparatively unrestricted, there would always be a temptation to exercise the control in response to the demands of various pressure groups. There is, furthermore, a serious question whether private international investment would ever revive in a world in which sweeping measures of exchange control might be applied to it by groups of countries at any time.

Other policy commitments under the plan

Another promise that all countries, including the United States, would make under the plan would be to give consideration to the views of the Fund on any existing or proposed monetary or economic policy, the effect of which would be to bring about sooner or later a serious disequilibrium in the balance of international payments.

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Each country will also be committed to furnish the Fund all the information it needs for its operation and particularly such reports as it may require in the form and at the times requested by the Fund.

The commitment to maintain exchange rates fixed by the Fund (giving the Fund control over the values of national currencies in terms of one another and of gold) has already been discussed in earlier sections of this memorandum. It is a major commitment as is also the agreement on the part of all members that the assets of the Fund located in their countries shall be free from any restrictions as to their use. If this is taken literally the Fund could invest its resources, sell them again, and generally engage in credit operations without restriction; but elsewhere most of these operations are made subject to the consent of the Board representative of the country involved and to a 4/5 vote. How consent could be refused in view of the binding assurance given in advance that there will be no interference with the freedom of the Fund is not made clear in the draft. The United States power to veto a 4/5 vote would, however, be definite.

Termination of membership in the Fund

These policy obligations which each member will assume will be fully as important as its financial obligations to the Fund. They will be more difficult to enforce. Financial obligations will largely take the form of local currency debts to the Fund, and local currency should be comparatively easy for a country to supply. Yet it is only for failing to meet its financial obligations that a country can be dropped from membership. If it is dropped, it gets back immediately its contribution minus any sum it owes the Fund.

A country may also withdraw voluntarily; but in this case it must give 2 years' notice and the Fund is given 5 years in which to liquidate its obligations to the withdrawing country. It is not clear how the Fund would pay the United States if this country withdrew because it felt that the dollar resources of the Fund were being wasted and it objected to being put in a hole by insistent requests that it should supply more dollars. Clearly the Fund in these circumstances would have no dollars with which to pay. The plan does not specify, however, that the Fund must pay in gold or dollars. Conceivably this country would find itself left with a mass of foreign currencies for which it had no use.

Present status of the plan

On January 21 Mr. Gardner sent to Mr. White and Mr. Berle a series of critical comments with respect to the December 24 draft. A copy is attached. Many of the points have already been covered in this memorandum. While a new version of the Treasury plan has been received just as this memorandum is being brought to a close (evening of January 29), a quick glance indicates that it is still a pretty defective piece of work. Mr. Berle's comments after reading the questions on the December 24 draft (most of which, together with some new ones, apply to the current version) was that "plainly, there is plenty of technical work to be done before we are through with this".

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Nevertheless it appears that the decision taken December 15 holds. Secretary Hull's consent has now been obtained to starting discussions with other countries at the technical level. The British have been told they can go ahead with similar discussions on their own plan in London. Presumably Messrs. White and Berle (with perhaps some other State Department people) will carry on the discussions here. In view of the effects that the project, as it shapes, may have upon the Federal Reserve System, the System might with reason request that one of its men should participate in these discussions. If this is not done, then there should be a definite arrangement to insure that Mr. White (or Mr. Berle) will report promptly and adequately to the committee members the viewpoints developed at the meetings with the foreign technicians. Past experience offers little hope that such reports will be forthcoming on any regular basis unless the committee insists.

Attachment

WRG

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